MONTANA MONEY SCHOOL

State Auditor John Morrison

Test Your Investing IQ - Answers

Circle the best answer.

1. A - Why?

Historically, investing in the stock market has yielded a greater return over time than bonds or traditional savings accounts at banks. Of course, in the short term, the stock market can have big ups and downs. If Joe plans to invest for the long term (20, 30, 40 years or more) the stock market will most likely give him the greatest return on his money. Even if a young person experiences a few years of loss in the market early on, they should be able to recover in time for retirement.

2. C - Why?

<u>Mary's current financial situation.</u> It says Mary has enough money to live on, but she may not have much to spare. If she invests in something that is too risky, Mary may lose money that she needs to buy food, pay rent or buy medicine.

<u>Mary's age.</u> Since Mary is in her 70s and no longer has an income from a job, she is relying on her retirement savings. If Mary were to suffer a significant loss with an investment, she may not be able to recover financially by relying on the stock market or interest rates to improve.

<u>The dot.com.</u> As the market has shown over the past few years, investments in start-up Internet companies can be very risky. While her heart may be in the right place in wanting to invest in her former students' company, she faces the risk of losing all of her investment (principal).

<u>The CD.</u> While a CD is usually a good investment for preserving principal, this is different. It has a 30-year maturity date. The question noted that Mary's goal is to have additional income in a few years to pay for housing and medical expenses - a short-term investment goal (maybe 5 or 10 years). If Mary chooses the CD, she cannot withdraw any principal until she is 100 years old. If she withdraws money earlier, she would risk paying penalties. The penalties could be expensive and that is money she can't recover.

<u>The "callable" part.</u> With a callable, or brokered CD, the issuer of the CD may be the only one to "call" in the CD. Some investors have misunderstood "callable" to mean that the maturity date of the CD is only one year. When the investors try to cash in their CD after a year, they find out about the long maturity date. If they really need their money, their only option is to cash in the CD early and face expensive penalties.

Neither of these investments are suitable for Mary based on the information we have been given. She should continue to investigate other investment opportunities.

3. C - Why

Selling unregistered securities is a crime in Montana. You must submit your investment offering to the Securities Department for review BEFORE you solicit any investors. If you were to do a "general solicitation" to attract potential investors without contacting our office first, the Securities Commissioner could charge you with selling unregistered securities and for selling securities without a license.

4. A - Why

All investments involve some risk. You may lose all of your money or you may suffer a small loss because interest rates went down or the stock market hit a slump. Most investments are not insured against loss. It is the risk you take.

Deposit accounts at banks are FDIC insured, but investments, even the ones sold at banks, do not qualify for this protection.

The SEC is a regulatory agency and can help you if you lost money because of unethical or illegal business practices on the part of your broker or the company you invested in. The SEC does not insure or protect against loss like the FDIC does.

If your broker (or salesperson for the company in which you want to invest) promises that your investment will be insured against loss - BEWARE. This may be a red flag for fraud. Contact the Montana Securities Department in the State Auditor's Office to learn more about the company before you commit to an investment.

5. B - Why

The main role of the federal and state securities regulators is to require that companies DISCLOSE information to potential investors about the risks of investing. Companies and/or investment brokers are required to conduct business honestly and fairly, but it is up to YOU, the investor, to make the final decision about how to best manage your money.

As in #4, if someone promises that you will not lose any money, BEWARE.

If a company is found guilty of illegal (or unethical) business practices, securities regulators can assess fines and a judge may order that restitution be paid to victims but most of the time, investors who fall to fraud only see pennies on the dollar of the original investment.

MONEY SCHOOL
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